

Crypto-
currency--
State Tax
Issues

MTC Nexus Committee

August 1, 2022

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What is a cryptocurrency?

Oxford Dictionary: a digital currency in which transactions are verified and records maintained by a decentralized system using cryptography, rather than by a centralized authority.

Author(s) under pseudonym of Satoshi Nakamoto published whitepaper in 2008 that established cryptocurrency as an open-source software program.

Bitcoin is considered the original cryptocurrency, created in 2009, and is currently the most popular and valuable (\$20,408/BTC on 7/14/22). Other popular ones: Ethereum (\$1143/ETH), Dogecoin (\$.06/DOGE), Solana (\$35/SOL).

How blockchain works with cryptocurrency

- Blockchain: network of computers (nodes) running a software program that creates a distributed ledger to which all nodes have access and on which cryptocurrency transactions are recorded after validation (mining) by the nodes.
- Mined transactions are recorded in chronological order in linked non-alterable data blocks.
- Transactions are pseudonymous--parties' public keys (analogous to party's email address or username) are shown in publicly accessible blockchain, but party-identifying information is not shown.
- Mining involves competition between nodes to be the first in solving cryptographic formulas to validate transactions forming a data block, requiring large computing capacity. Successful miner is rewarded with additional cryptocurrency.

Steps to buy or sell cryptocurrency

Investopedia:

- 1. Establish an account with a cryptocurrency venue, such as a cryptocurrency exchange (examples: Coinbase, Kraken, Gemini, FTX)
- 2. Link account to a payment method (bank acct., credit card, etc.)
- 3. Place buy/sell order
- 4. Store purchased cryptocurrency in a wallet (“hot” or “cold”)

Cryptocurrency Tax Guidance

IRS: Notice 2014-21

Rev. Rul. 2019-24

IRS treats cryptocurrency as “property,” not “currency,” so buying or selling it generates capital gains/losses.

State tax guidance:

NY, NJ, WI have published state income tax guidance, based on the IRS. UT, CO are working to accept cryptocurrency for tax payments. KS published sales tax guidance. PA, WA published NFT sales tax guidance.

Cryptocurrency Exchange Reporting

- H.R. 3684 (P.L. 117-58) Infrastructure Investment and Jobs Act imposes new reporting requirements on cryptocurrency exchanges/brokers effective 1/1/2023, with reports containing detailed transaction information concerning gains/losses to be provided to IRS and investors after year end.